

BILL ANALYSIS

S.B. 1442
By: Fraser
Business & Industry
Committee Report (Unamended)

BACKGROUND AND PURPOSE

The Business Organizations Code, adopted in 2003 by the 78th Texas Legislature, was a joint project of the Business Law Section of the State Bar of Texas and the Office of the Texas Secretary of State, with assistance in editing and drafting coming from the Texas Legislative Council. The 79th and 80th Texas Legislatures passed several amendments to the Business Organizations Code.

The Business Organizations Code codified the provisions of prior law found in the Texas Business Corporation Act, the Texas Nonprofit Corporation Act, the Texas Miscellaneous Corporation Laws Act, the Texas Limited Liability Company Act, the Texas Revised Limited Partnership Act, the Texas Real Estate Investment Trust Act, the Texas Uniform Unincorporated Nonprofit Associations Act, the Texas Professional Corporation Act, the Texas Professional Associations Act, the Texas Revised Partnership Act, the Cooperative Associations Act, and other existing provisions of Texas statutes governing domestic entities.

S.B. 1442 builds on the Business Organizations Code's progression and proposes several technical and substantive amendments. These amendments correct errors, fill gaps in coverage, eliminate redundant and antiquated provisions, and conform language of the code to the language of source statutes. The bill authorizes the formation of series limited liability companies, sets forth provisions for the continuance of an entity after conversion, and authorizes emergency provisions to be included in the governing documents of a company. The bill also amends the Business & Commerce Code to set forth provisions regarding a foreign filing entity, the Texas Professional Association Act, and the Texas Revised Limited Partnership Act.

RULEMAKING AUTHORITY

It is the committee's opinion that this bill does not expressly grant any additional rulemaking authority to a state officer, department, agency, or institution.

ANALYSIS

S.B. 1442 amends the Business Organizations Code to redefine "conversion" by specifying that it refers to a continuance of a domestic entity as a non-code organization, rather than as a foreign entity, of any type, and to a continuance of a non-code organization, rather than a foreign entity, as a domestic entity of any type. The bill expands the definition to include the continuance of a domestic entity of one type as a foreign entity of the same type that may be treated as a domestication, continuance, or transfer transaction under the laws of the jurisdiction of formation of the foreign entity, and the continuance of a foreign entity of one type as a domestic entity of the same type that may be treated as a domestication, continuance, or transfer transaction under the laws of the jurisdiction of the formation of the foreign entity. The bill redefines "converted entity" and "converting entity" to change references of "entity" to "organization" in the definitions. The bill defines "non-United States entity" and "non-United States jurisdiction." The bill redefines "shareholder" or "holder of shares" to include the beneficial owner of shares issued by a for-profit corporation, whose shares are held in a voting trust or by a nominee on the

beneficial owner's behalf, to the extent of the rights granted by a nominee statement on file with the for-profit corporation.

S.B. 1442 removes the prohibition against a domestic entity operating as a railroad company. The bill prohibits a certificate representing an ownership interest in a domestic entity from being issued in a bearer form. The bill authorizes the governing persons, owners, or members of a domestic entity to adopt certain provisions in the entity's governing documents for the management of the entity during an emergency, which is considered to exist if a majority of the entity's governing persons cannot readily participate in a meeting because of a catastrophic event, and sets out the effects of the emergency provisions.

S.B. 1442 establishes that a certificate issued by the secretary of state stating that a domestic filing entity is in existence may be relied on as conclusive evidence of the entity's existence and that a certificate issued by the secretary of state stating that a foreign filing entity is in existence or registered may be relied on as conclusive evidence that the entity is registered and authorized to transact business in Texas. The bill specifies that such reliance is subject to any qualification stated in the certificate. The bill specifies that a certificate of correction to correct an inaccurate filing instrument must be signed by the person authorized by law to sign the filing instrument to be corrected, rather than the person authorized to act on behalf of the entity. The bill provides that the participation or attendance at a meeting of the owners, members, or governing persons of a domestic entity by a person entitled to notice of the meeting constitutes a waiver by the person of notice of a particular matter at the meeting that is not included in the purposes or business of the meeting described in the notice unless the person objects to the matter when it is presented. The bill provides that, except as otherwise provided by an entity's governing documents, an electronic transmission of a consent by an owner, member, or governing person of a filing entity to the taking of action by the entity is considered a signed writing if the transmission contains or is accompanied by information from which it can be determined that the electronic transmission was transmitted by the owner, member, or governing person and the date on which the owner, member, or governing person transmitted the electronic transmission, unless the consent is otherwise dated.

S.B. 1442 sets out the requirements for supplemental information that must be included in an application for registration of a foreign limited liability company governed by a company agreement that establishes or provides for the establishment of certain designated series of members, managers, membership interests, or assets that has certain characteristics. The bill requires a foreign filing entity that is a limited partnership to amend its registration to reflect the admission of a new general partner, the withdrawal of a general partner, and a change in the name of the general partner stated in its application for registration. The bill makes clarifying changes to a provision relating to the certificate from the comptroller of public accounts about the payment of certain taxes that must be filed with the voluntary withdrawal of registration by a foreign filing entity or foreign limited liability partnership, and removes references to a foreign for-profit corporation and a foreign limited liability company. The bill provides that a foreign filing entity or foreign limited liability partnership registered in Texas that converts to a domestic filing entity is considered to have withdrawn its registration on the effective date of the conversion. The bill makes clarifying changes to a provision relating to the tax clearance letter a foreign filing entity must file with a certificate of reinstatement and removes references to a foreign for-profit corporation and a foreign limited liability company. The bill includes owning, without more, real or personal property in Texas in the activities that do not constitute a transaction of business in Texas.

S.B. 1442 authorizes a converting entity to elect to continue its existence in its current organizational form and jurisdiction of formation in connection with the entity's conversion as a domestic entity of one organizational form into a non-United States entity of the same organizational form, or its conversion as a non-United States entity of one organizational form into a domestic entity of the same form. The bill makes a provision prohibiting the acceptance of a certificate for filing under certain circumstances inapplicable in connection with filing a

certificate of conversion if the converting entity is a domestic filing entity that elects to continue in existence. The bill exempts a non-United States entity that also exists as a domestic filing entity because of a conversion and election to continue its existence from provisions that govern foreign entities. The bill requires the election for the converting entity to continue its existence in its current form and jurisdiction to be adopted and approved as part of the conversion plan as required by applicable provisions relating to conversions and permitted by, or not prohibited by and inconsistent with, the laws of the applicable non-United States jurisdiction. The bill requires a converting entity that elects to continue its existence to include a statement certifying that elected continuance in the entity's plan of conversion. The bill sets out special provisions relating to the applicability of other laws to the converting entity after the conversion, as well as the rights, titles, and interests in property owned by the entity and its liabilities and obligations. The bill requires such an entity to file a "Certificate of Conversion and Continuance" and to include a statement certifying the entity's elected continuance.

S.B. 1442 authorizes the beneficial owner of an ownership interest subject to dissenters' rights held in a voting trust or by a nominee on the beneficial owner's behalf to file a petition requesting a finding and determination of the fair value of the owner's ownership interest if no agreement between the dissenting owner of the ownership interest and the responsible organization has been reached within a period of at least 60 days from the date the offer is first delivered to the dissenting owner. The bill establishes that when the beneficial owner files the petition, the beneficial owner shall at that time be considered the owner, the dissenting owner, and the holder of the ownership interest, and the dissenting owner who demanded payment has no further rights regarding the ownership interest. The bill entitles a dissenting owner, on the termination of the right to dissent, to receive the same consideration received by owners of the same class and series of ownership interests held by the owner, as if no action for fair value payment was taken, if the owner's ownership interests were canceled, converted, or exchanged as a result of the action or a subsequent action, and provides that any action taken by the domestic entity after the date of the demand for payment by the owner to perfect the owner's rights of dissent and appraisal will not be considered ineffective or invalid because of the restoration of the owner's ownership interests or other rights or entitlements of the owner. The bill clarifies that the dissenting owner is entitled to receive dividends or other distributions made after the date of the owner's payment demand, rather than in the interim, to owners of the same class and series of ownership interests held by the owner as if the demand had not been made, subject to any change in or adjustment to the ownership interest because of an action taken by the domestic entity, rather than specifically the cancellation or exchange of the ownership interests, after the date of the demand.

S.B. 1442 requires a certificate of reinstatement for an involuntarily terminated domestic filing entity to be accompanied by a tax clearance letter from the comptroller stating that the filing entity has satisfied all franchise tax liabilities and may be reinstated, if the entity is eligible for assessment of franchise taxes and is not a nonprofit corporation. The bill clarifies that the principal place of a domestic partnership or limited liability company is the entity's principal place of business in Texas, for purposes of determining jurisdiction for the winding up and termination of the entity. The bill authorizes the secretary of state to issue a certificate, a letter, or both to evidence or acknowledge the filing of an instrument authorized to be filed with the secretary, and makes this provision and provisions relating to information disclosed by interrogators and relating to appeals from the secretary of state inapplicable to a domestic real estate investment trust.

S.B. 1442 requires a for-profit corporation's certificate of formation to authorize one or more classes or series of shares that together have unlimited voting rights and one or more classes or series of shares, which may be the same class or series of shares as those with voting rights, that together are entitled to receive the net assets of the corporation on winding up and termination. The bill makes conforming changes relating to this requirement. The bill authorizes a for-profit corporation to place shares in escrow, although the shares are fully paid and nonassessable, or make other arrangements to restrict the transfer of the shares, if the shares are issued for

consideration consisting wholly or partly of a contract for future services or benefits or a promissory note, and authorizes credit distributions made with respect to the shares against their purchase price, until the services are performed, the note is paid, or the benefits are received. The bill authorizes the corporation to pursue certain remedies if the services are not performed, the note is not paid, or the benefits are not received. The bill removes language that allows the scrip issued by a for-profit corporation that entitles the holder to receive a certificate for a full share or an uncertificated full share on the surrender of the scrip aggregating a full share to be issued in bearer form.

S.B. 1442 provides that shares that are issued by a for-profit corporation are outstanding shares unless the shares are treasury shares or are canceled and provides that, if there are outstanding shares, one or more shares that together have unlimited voting rights and one or more shares that together are entitled to receive the net assets of the corporation on the winding up and termination of the corporation must be outstanding shares. The bill authorizes a for-profit corporation to establish a procedure by which the corporation recognizes as a shareholder the beneficial owner of shares registered in the name of a nominee and sets out requirements for the procedure. The bill clarifies a provision relating to the preemption of liability of an affiliate of a for-profit corporation for an obligation with limited liability. The bill amends a provision that sets out the voting options for shareholders entitled to vote in each election of a for-profit corporation's directors to clarify that the option of cumulative voting exists only if expressly authorized by the corporation's certificate of formation in general or with respect to a specified class or series of shares or group of classes or series of shares and subject to certain limitations. The bill amends a provision allowing a for-profit corporation's certificate of formation to provide that directors are entitled to cast more or less than one vote on specified matters to extend that entitlement to votes on all matters, and specifies that such a provision entitles directors voting in any committee or subcommittee to cast more or less than one vote regarding all matters or the specified matters, as applicable, unless otherwise provided by the certificate of formation. The bill includes as a form of authorization of a contract or transaction involving interested directors or officers of a for-profit corporation that the officer or director signs, in the person's capacity as a director or committee member, a unanimous written consent of directors or committee members, and makes clarifying and conforming changes to this provision.

S.B. 1442 expands the provisions relating to the required membership of a limited liability company in provisions that may not be waived or modified in its company agreement. The bill provides that certain provisions governing the rights of a third party in a secured transaction do not apply to a membership interest in a limited liability company and establishes that this provision controls in any conflict with those laws. The bill provides that it is the express intent of this provision to permit the enforcement, as a contract among members of a limited liability company, of any provision of a company agreement that would otherwise be ineffective under the provisions governing the rights of a third party in a secured transaction. The bill prohibits the foreclosure of a charging order lien on a judgment debtor's membership interest in a company. The bill amends a provision that prohibits a limited liability company from making a distribution to a member of the company under certain conditions to specify that the term "distribution" does not include an amount constituting reasonable compensation for present or past services or a reasonable payment made in the ordinary course of business under a bona fide retirement plan or other benefits program. The bill authorizes a limited liability company agreement to establish or provide for the establishment of a record date with respect to allocations and distributions. The bill includes as a form of authorization of a contract or transaction involving interested governing persons or officers of a limited liability company that the governing person or officer signs, in the person's capacity as a governing person or committee member, a written consent of governing persons or committee members, and makes clarifying and conforming changes to this provision.

S.B. 1442 authorizes the creation of a series limited liability company by allowing a limited liability company agreement to establish or provide for the establishment of one or more designated series of members, managers, membership interests, or assets that has separate rights,

powers, or duties with respect to specified property or obligations of the company or profits and losses associated with specified property or obligations, or that has a separate business purpose or investment objective. The bill sets out provisions relating to the enforceability of the obligations and expenses of a series against its assets, the holding of assets associated with a series, and the requirements for a notice of limitation on the liabilities of a series. The bill establishes the general powers of a series; provides that a member or manager associated with a series or a member or manager of the company is not liable for a debt, obligation, or liability of a series unless the company agreement specifically provides otherwise; and allows the company agreement to expand or restrict any duties, including fiduciary duties, and related liabilities that a member, manager, officer, or other person associated with a series has to the series or the company, a member or manager associated with the series, or a member or manager of the company. The bill authorizes the company agreement to establish classes or groups of members or managers associated with a series and sets forth provisions relating to the governing authority of a series, the effect of certain events on a manager or member with respect to a series, the status of a member with respect to a distribution, the establishment of a record date for allocations and distributions, and the making of distributions with respect to a series. The bill establishes that the provisions of law related to limited liability companies apply to a series limited liability company and its associated members and managers, to the extent the provisions governing each company are not inconsistent. The bill authorizes a series and its business and affairs to wind up and terminate without causing the winding up of the company and provides that the series terminates on the completion of the winding up process. The bill specifies the conditions that require the winding up of a series and sets out procedures for the winding up and termination. The bill provides for the revocation of a voluntary winding up, the cancellation of an event requiring a winding up, the authority of a series to continue business following either situation, and the winding up by order of a district court with appropriate jurisdiction.

S.B. 1442 authorizes a limited liability partnership to have elected or appointed officers. The bill specifies that a partner's protection from personal liability in a limited liability partnership applies to personal liability to any person, including a partner, and includes as an exception to such protection any liability provided in the partnership agreement. The bill requires a certificate from the comptroller to be filed with a notice of the withdrawal of a domestic or foreign partnership's registration stating that all state taxes administered by the comptroller have been paid by the partnership. The bill requires a tax clearance letter from the comptroller stating that a foreign partnership has satisfied all franchise tax liability and may be reinstated to be filed with the partnership's certificate of reinstatement.

S.B. 1442 amends a provision that limits a limited partnership's distribution to a partner to specify that the term "distribution" does not include an amount constituting reasonable compensation for present or past services or a reasonable payment made in the ordinary course of business under a bona fide retirement plan or other benefits program. The bill prohibits the foreclosure of a charging order lien on a judgment debtor's partnership interest. The bill specifies that the secretary of state has the authority to terminate the certificate of formation of a domestic limited partnership or revoke the registration of a foreign limited partnership, rather than cancel those credentials, and makes conforming changes. The bill includes as a condition for a limited partnership's reinstatement of its certificate or registration by the secretary of state that the limited partnership has paid all taxes, penalties, and interest due and accruing before the termination or revocation of the certificate or registration.

S.B. 1442 provides that certain provisions governing the rights of a third party in a secured transaction do not apply to a general or limited partnership interest in a company and establishes that this provision controls in any conflict with those laws. The bill specifies that it is the express intent of this provision to permit the enforcement, as a contract among the partners of a partnership, of any provision of a partnership agreement that would otherwise be ineffective under those laws governing the rights of a third party in a secured transaction.

S.B. 1442 includes as a form of authorization of a contract or transaction involving interested trust managers or officers of a real estate investment trust that the trust manager or officer signs, in the person's capacity as a trust manager or committee member, a unanimous written consent of trust managers or committee members, and makes clarifying and conforming changes to this provision.

S.B. 1442 amends the Business & Commerce Code to modify several definitions and in other provisions to remove references to a limited liability partnership as a registered limited liability partnership. The bill amends the definitions of the terms "company" and "person" to include a foreign filing entity and includes such an entity's registered office and principal office under the definition of the term "office." The bill defines the term "foreign filing entity" as an entity formed under the laws of a jurisdiction other than this state that registers or is required by law to register with the secretary of state to conduct business or render professional services in Texas under state laws governing foreign entities. The bill includes a foreign filing entity, or its shareholders, associates, partners, or members, in those parties that are not required to file a certificate to conduct business or render a professional service in Texas under the name of the entity as stated in the certificate of formation, application filed with the secretary of state, or other comparable document of the entity. The bill also includes a foreign filing entity in provisions requiring a person or certain types of business entities to file a certificate for an assumed business or professional name if the person or entity regularly conducts business or renders a professional service in Texas under an assumed name. The bill removes references to a corporation in provisions that specify the information that must be stated in such a certificate. The bill specifies that the certificate requires a statement that the registering entity is a for-profit corporation, if applicable, rather than that the entity is a business corporation and removes a provision that requires such a certificate to include the address of the registrant's registered office in Texas and the name of its registered agent at that address and makes conforming changes. The bill amends provisions that establish the place of filing such a certificate. The bill removes from the events that would cause the information in a certificate to become materially misleading a change in the address of the office or in the identity of the agent for a registrant required by law to maintain a registered office or similar office and a registered agent or similar agent at that office.

S.B. 1442 amends the Texas Professional Association Act to provide that a certificate from the comptroller stating that all state taxes administered by the comptroller have been paid must accompany the original and a copy of the articles of dissolution of a professional association that must be delivered to the secretary of state.

S.B. 1442 amends the Texas Revised Limited Partnership Act to include in the required actions to cancel a certificate of a limited partnership or the registration of a foreign limited partnership the submission, with the secretary of state, of a certificate from the comptroller stating that all state taxes administered by the comptroller have been paid.

S.B. 1442 repeals Section 2.006, Business Organizations Code, relating to the permissible purpose of a for-profit corporation related to railroads.

EFFECTIVE DATE

September 1, 2009.